United States Court of Appeals
for the Second Circuit

APPELLANT'S BRIEF

ORIGINAL

To Be Argued By
GABRIEL KASZOVITZ

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

75-7288

NATHAN CHANOFSKY,

Plaintiff-Appellant,

-against-

THE CHASE MANHATTAN CORPORATION,

Defendant-Appellee.

UNITED STATES COURT OF APPEALS
FILED
AUG 26 1975

ON APPEAL FROM THE UNITED STATES
DISTRICT COURT FOR THE SOUTHERN
DISTRICT OF NEW YORK

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PLAINTIFF-APPELLANT'S BRIEF

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
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NATHAN CHANOFSKY,

Plaintiff-Appellant,

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---------------------------------- X

PLAINTIFF-APPELLANT'S BRIEF

ISSUES

1. Did the Court below incorrectly apply the 'out-of-pocket' measure of damages rule in a 10b-5 stock fraud action? (POINT I)

2. Was it error for the lower Court to ignore the immediate and decisive market reaction to Chase's curative announcement; and other relevant market action? (POINT II)

3. May a 10b-5 stock fraud action be maintained only if the fraud caused the market price of the securities to be "grossly unfair?" (POINT III)

4. Is the requirement that the market price

be "grossly unfair" imposed by the Court below, contrary to the provisions of Section 28a of the Securities Exchange Act of 1934 mandating recovery for "actual damages?" (POINT III)

5. Did the Court below err in holding the following facts material:

(a) that the non-disclosed losses in defendant's bond trading inventory were "unrealized"?

(b) that such losses were a small percentage of defendant's total assets,? and

(c) that the losses were subsequently reduced?

(POINT IV)

6. As between the wrongdoer and the defrauded party, should the wrongdoer be permitted to be the beneficiary of a "windfall" in the form of a subsequent fortuitous rise in the market prices of the securities, so as to shield the wrongdoer from liability for its acts? (POINT V)

7. Is a defrauded purchaser in a Rule 10b-5 stock fraud action precluded from recovery because of a subsequent rise in the market prices of the

securities, even though the rule of damages requires that the loss be the difference between the price paid and the 'actual' or 'real' value at the date of purchase? (POINTS I, II and V)

8. Did the Court below err in making Rule 52 findings of fact as if the action had been tried, when, in fact, there had been no trial or waiver of a trial? (POINTS VI and VII)

9. Did the existence of triable factual issues on the question of damages preclude summary disposition of this case on motion? (POINT VII)

10. Is the waiver of a jury binding where it is not made in accordance with the requirements of Rule 39? (POINT VIII)

STATEMENT

This is a class action for money damages arising out of defendant's violations of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. Section 78(j)(b), and Rule 10(b)(5) promulgated thereunder by the Securities and Exchange Commission.

The Defendant's Wrongdoing

In discussing the legal consequences of defendant's wrongdoing, the Court should have in mind the wrongdoing complained of.

As recited in the Wall Street Journal:

> "Chase Manhattan Corp.'s earnings gains this year have been wiped out by the discovery that certain of its securities holdings were valued at falsely high levels." (53)*

David Rockefeller, Chairman of the Chase Manhattan Corporation, characterized the events as follows:

> "There is no question but that extremely serious errors in judgment have been made.... The resignation of the senior vice-president in charge of Chase's bond-dealer account activities has been accepted as of October 1." (53,54)

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* All references to page numbers are those in the appendix.

The Wall Street Journal article continues:

> "Sources close to Chase said the false valuations were 'apparently deliberate' but that no law enforcement agency had been called in. The false entries 'weren't accidental,' the source said." (53)

The Wall Street Journal article then discusses the culpability not only of the Chase employees, who were believed to have made the false entries, but the culpability of Chase itself for permitting those false entries to go undetected for a period of nine months.

> "Analysts generally expressed surprise that the false entries could have gone undetected for nine months. Most banks and non-bank dealers have control systems under which securities valuations are made on a weekly, monthly or quarterly basis by persons outside the actual trading operation. This serves as a check against valuations by specific traders or their superiors.
>
> "In Chase's case, sources said that monthly checks were made, but the checks were carried out by the trading department itself. Periodic audits were also made by outsiders, but relatively infrequently, as indicated by the nine-month wait since the last previous one.
>
> "Mr. Rockefeller said immediate steps had been taken to establish 'additional controls' over bond-trading account valuation procedures. According to a bank spokesman, the valuations will be audited monthly by persons outside the department and at times by outside accounting firms." (53)

<u>The Market's Response to the Curative Disclosure</u>

Defendant Chase has three outstanding issues of

equity securities (42): (a) common stock, (b) the 6-1/2% convertible debentures held by the plaintiff and convertible into Chase's common stock, and (c) the 4-7/8% convertible debentures issued by the defendant's wholly owned banking subsidiary, which are also convertible into the defendant's common stock. (42)

Plaintiff submitted a number of schedules showing closing prices on the New York Stock Exchange over a six week period for the following securities and market indices:

(a) Chase's common stock, the common stocks of two other bank holding companies (Chemical and Morgan) deemed comparable by defendant (25), and of Citicorp, which is also a comparable bank holding company. (43,44)

(b) Chase's 6-1/2% convertible debentures and Chase's 4-7/8% convertible debentures, the convertible debentures of Chemical and Morgan (deemed comparable by defendant) (25), and a series of Chase's capital notes which have no conversion rights. (45, 46)

(c) Bank of New York convertible debentures, Standard & Poor's industrial index of 425 stocks, and two New York Stock Exchange indices, the

composite index and the financial index, all of which are included to show that the pertinent market prices shown in the other two schedules were not aberrations, but true indications of trading in bank securities and the market generally during the period in question. (56)

These schedules show the impact that the Rockefeller statements, released on October 2, 1974, had on the market prices of all three Chase equity securities, including both series of Chase's convertible debentures. That impact was an immediate and clear decline in the price of all three securities for a period of three days after the Rockefeller statement. Chase's common stock dropped 3-1/2 points, the 6-1/2% debentures dropped 2-1/2 points, and the 4-7/8% debentures dropped 4 points. (44-46) These schedules also show that during that same three day period there was no similar decline in the market prices of the comparable securities (with one exception) or in the market indices. (44-46, 56)

Finally, these schedules also show that although the three Chase equity securities in question rose in price after October 4, 1974, that rise was

part of a general market advance at the time. The rise in the market prices of all of the comparable securities (Morgan common stock and convertible debentures, Chemical common stock and convertible debentures, and Citicorp common stock) after October 4, 1974, took them all to levels above those prevailing for those securities prior to the Rockefeller announcement on October 2, 1974. On the other hand, the advance in the market prices of the Chase common stock and both series of Chase's convertible debentures took them only to the levels they were at before the Rockefeller disclosure.

The Proceedings in the Court Below

Before issue was joined the defendant moved to dismiss the complaint pursuant to Rule 12(b)(6) on the ground that it failed to state a claim on which relief can be granted, or in the alternative, for summary judgment pursuant to Rule 56. (17-18) The theory underlying defendant's motion can be summarized as follows: (21-39)

(a) Because the conversion premium for Chase's 6-1/2% convertible debentures was approximately 25% (41), these convertible debentures did not contain any equity characteristics.

(b) Because the Chase 6-1/2% convertible debentures did not contain equity characteristics, the market prices for these securities responded only to interest rates and the financial condition of Chase. That is, they traded as a straight bond.

(c) Because of Chase's strong financial condition, there could be no doubt as to Chase's ability to meet its obligations to pay the interest and principal on these convertible debentures.

(d) Consequently, the Rockefeller curative disclosure could not have had any effect on the market price of Chase 6-1/2% convertible debentures.

(e) Because the 6-1/2% convertible debentures did not contain any equity characteristics, plaintiff could not be a class representative for the common stockholders.

Although defendant sought to have the complaint dismissed as a matter of law, Judge Duffy proceeded to make factual findings and legal conclusions pursuant to Rule 52 on the erroneous assumption that the parties "waived any... offer of proof." (102-3) On its motion seeking reargument, plaintiff denied that it had made any such waiver of proof, or agreed to submit the whole case for determination at oral argument (82-83).

POINT I

JUDGE DUFFY INCORRECTLY APPLIED THE 'OUT OF POCKET' RULE OF DAMAGES WHICH A DEFRAUDED PURCHASER IS ENTITLED TO RECEIVE UNDER RULE 10 b-5

Judge Duffy dismissed plaintiff's complaint on the basis of his factual determination that plaintiff suffered no damages.* Judge Duffy states: (105)

> "Chase also contends that the plaintiff suffered no damage. It is sufficient for me to deal only with this latter claim.
>
> "It is important to note that plaintiff still holds the debentures which he purchased and that according to the tables produced to this Court it appears that plaintiff has now made a 'paper profit' from the transaction..."

In reaching his decision, Judge Duffy quotes the rule of damages applicable in this case to be the following:

"The rule of damages has been summarized

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* On a motion pursuant to Rule 12(g)(6) or Rule 56, the material facts as alleged in plaintiff's complaint are deemed admitted for the purposes of defendant's motion. Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 355 F. Supp. 264, 268 (S.D.N.Y. 1971), aff'd 495 F. 2d 228 (1974). Therefore, defendant Chase's wrongdoing must be assumed for the purpose of this appeal.

and analyzed in a Note entitled <u>Damages in Rule 10 b-5 Cases,</u> 26 Stanford Law Review, 371 (Jan. 1974), which states:

"The out-of-pocket measure of damages 'is the difference between the contract price, or the price paid, and the real or actual value at the date of sale, together with such outlays as are attributable to the defendant's conduct.' Such a formula has no tolerance for inclusion of a speculative factor in its compensation scheme. The guiding philosophy is 'not what the plaintiff might have gained but what he has lost.' " [Emphasis in original.] (107)

Judge Duffy then concluded: (108)

"Here plaintiff never sold his debentures. He has no 'out-of-pocket' loss. Any damages awarded would have to be based on mere speculation, guess or conjecture..."

Although Judge Duffy recognizes the correct damages rule, he fails to apply it. Judge Duffy erroneously measures a defauded purchaser's damages as the difference between the price the purchaser paid and the proceeds he receives upon sale, or, if the securities are not sold, then the difference between the price paid and the value of the securities at the time of the Court hearing. That Judge Duffy did in fact so erroneously apply the damages rule is evidenced by his treating as dispositive of the question of damages, the facts that plaintiff never sold his debentures and that at the time of oral argument, plaintiff had made a "paper profit."

It may be that Judge Duffy's misapplication of the damages rule stems from his erroneous interpretation of the "date of sale" language in the rule which he relies upon. Obviously "the date of sale" to which Judge Duffy looked was the date the defrauded purchaser disposed of his securities (or absent a sale, market price at the date of the Court hearing). In fact, "the date of sale" intended by the rule in a defrauded purchaser situation is the date the purchaser acquires the securities, and not the date he disposes of them. The reference to "date of sale" in the rule is not an inartful use of language, but is a shorthand reference to the critical date that covers both the defrauded seller and defrauded purchaser situations. It is only through such an error of date selection that any significance could be attributed, as Judge Duffy did, to the fact that "plaintiff never sold his debentures" and therefore had "no 'out-of-pocket' loss," (108) and the fact that plaintiff has made a "paper profit" (105)

The "out-of-pocket" measure of damages, correctly applied, is the difference between (a) the price paid, and (b) the true value of the securities at the time purchased. <u>Affiliated Ute Citizens v.</u>

United States, 406 U.S. 128, 155 (1972); Estates Counseling Service, Inc. v. Merrill Lynch Pierce Fenner & Smith, Inc., 303 F. 2d 527, 533 (10th Cir. 1962); Richardson v. MacArthur, 451 F. 2d 35, 43 (10th Cir. 1971); Hindman v. First National Bank, 112 F. 931, 936 (6th Cir. 1902); Levine v. Seilon, Inc. 430 F. 2d 328, 334 (2nd Cir. 1971). True value, or actual value has been defined in the Stanford Law Review article, supra, as follows:

> "Actual value equals 'real value' or 'the prices at which [the buyer] would have purchased the stock in an unmanipulated market.'..."

At no point in its opinion did the Court below address itself to the proof required to ascertain the "actual" or "real" value of the Chase securities at the date of plaintiff's acquisition, or in the class action, the "actual" or "real" values in the period during which the class members purchased their Chase securities. Consequently, its factual determination of "no damage" was not based on the real or actual value of the securities at the time of purchase.

POINT II

THE MARKET REACTION TO THE CURATIVE ANNOUNCEMENT IS THE PROPER MEASURE OF THE DEFRAUDED BUYER'S LOSS. IT WAS ERROR FOR THE LOWER COURT TO IGNORE THE IMMEDIATE AND DECISIVE REACTION TO CHASE'S CURATIVE ANNOUNCEMENT.

The measure of damages rule in a defrauded purchaser situation requires ascertaining as of the date of purchase, the difference between the price paid and the actual or real value of the securities purchased. Both the cases and the text writers have stated that the market reaction to the curative disclosure is highly probative of that difference.

In Esplin v. Hirschi, 402 F. 2d 94, 104 (10th Cir., 1968) the Court held:

> "The plaintiffs have incurred a loss as a result of the fraudulent practices of the defendants in the sale of securities in violation of the securities laws. The extent of this loss will not necessarily be fully known until some time after the original transaction. This follows because the same fraudulent practices that have induced the plaintiffs' purchase of the securities also operate on other buyers thereby affecting the prevailing market price. It is not until the existence of the fraudulent conduct is known that the true value of the securities as an investment can be ascertained."

See also, Richardson v. MacArthur, supra.

Bromberg, in his well-known treatise, Securities Law Fraud - S.E.C. Rule 10 b-5, states:

> ".... in open-market cases there may be independent evidence of materiality in the way price reacts when the information is disclosed, or corrected if it has been misrepresented. This suggests a more realistic test in terms of what the market did, instead of what would the market (implicitly reasonable) do. Such a test would better compensate for actual losses from foolish but dollar-measurable market reactions.... No doubt if there is a demonstrable market reaction, it will be taken into consideration." 2 Bromberg, Securities Law Fraud - S.E.C. Rule 10 b-5, Sec. 8.3, at page 201.

Courts have often looked to market reaction at the time of the curative disclosure to measure damages. See Reynolds v. Texas Gulf Sulphur Company, 309 F. Supp. 548, 564 (D.C. Utah, 1970), aff'd in part sub nom Mitchell v. Texas Gulf Sulphur Company, 446 F. 2d 90 (10th Cir. 1971).

The sudden drop in the market prices of the three Chase equity securities in reaction to the Rockefeller disclosure, is a proper measure for determining the amount of overpayment for such securities by plaintiff and other members of the class during the almost five-month period during which Chase's misleading quarterly financial statements were extant. For at least three days after the

Rockefeller disclosure, the market price of the comparable securities appeared to be relatively stable. Under such circumstances, the drop in the market prices of the three Chase equity securities pinpoint the immediate market reaction to the curative announcement.

This Court's attention is directed to the fact that in the two business days immediately preceding the Rockefeller public release, the market prices of the Chase securities had already declined. As a result, the decline in the larger 5 (business) day period was substantially greater than the 3-1/2 points for the common stock, the 4 points for the 4-7/8% convertible debentures, and the 2-1/2 points for the 6-1/2% convertible debentures. This earlier decline may have been the result of a leaking of this information into the market prior to the public announcement, a not uncommon phenomena. See Reynolds v. Texas Gulf Sulphur Company, supra.

The subsequent rise in the market prices of the three Chase equity securities after October 4, 1974, was less than the rise in the prices of the comparable securities and in the applicable market indices. Therefore, the damages in

this proceeding may be even greater than that recorded in the three day period ending October 4, 1974.

For the Court below to have ignored this clear and convincing reaction to the Rockefeller announcement in deciding the question of damages, was error.

It is submitted that these facts, the immediate drop in the market prices of the Chase equity securities in the three day period following the Rockefeller announcement, the possibility that an early leak of this information caused an earlier decline, and the subsequent greater advances of comparable securities, if they do not compel the conclusion that:

(a) the drop in the market prices of the Chase securities after the announcement measured the amount by which the prices of those three Chase securities had been inflated because of the misleading financial information extant during the almost five-month period preceding the curative announcement, and

(b) Chase's curative announcement created a permanent impairment in the market prices of the three Chase equity securities;

certainly raise factual issues to be resolved at a trial in which expert testimony on market activity can be presented and evaluated.

That conflicting inferences are available to a jury from the facts in this case, especially concerning market activity, is clear from the conflicting interpretation of the same facts proferred by plaintiff and defendant. For example, defendant submitted charts (65-73) on its motion to support its argument that the 2-1/2 point drop in the price of Chase's 6-1/2% convertible debentures during the three day period immediately following the release of the curative announcement was:

> "wholly within the expected range of price variances which frequently occur on a short term basis in an auction market... Such price fluctuations result from the normal dynamics of the market." (61,77)

However, Mr. Mark Sontag, a registered representative with a local securities firm, noted in his affidavit: (77)

> "But that is not the same thing as saying that all such fluctuations result from the normal dynamics of an auction market, or that the price movements of the three Chase securities during the period in question resulted from the normal dynamics of the market. On the contrary, the very close time proximity between the Rockefeller announcement and the price drops of the Chase securities, and the different market movements (and non-movements) of the comparable securities compel the conclusion that there was a causal relationship between the Rockefeller statement and the prices of the three Chase securities and that the Rockefeller statement had a negative effect on the market prices of the three Chase equity securities, including the 6-1/2% convertible debentures."

POINT III

THE COURT ERRED IN LIMITING 10 b-5 ACTIONS TO SITUATIONS WHERE THE MARKET PRICE WAS "GROSSLY UNFAIR"

Judge Duffy, in his opinion, sets forth, without authority, a new criteria for 10 b-5 actions (106): that the fraud complained of must make the market price of the security "grossly unfair" for an action to be maintained. To permit Judge Duffy's opinion on this point to stand would be to establish authority shielding wrongdoers from the consequences of their wrongful actions unless those actions have "grossly unfair" consequences, whatever that phrase may mean. Furthermore, Judge Duffy's "grossly unfair" language runs contrary to the language and intent of Sec. 28(a) of the Securities Exchange Act of 1934 which permits the recovery of "actual damages" and not "grossly unfair" damages. In this connection, it is noteworthy that the "actual damages" requirement of Sec. 28(a) is met by the "out-of-pocket" measure of damages applicable in 10 b-5 stock fraud actions. See Myzel v. Fields, 386 F. 2d 718 (8th Cir., 1967)

In limiting 10 b-5 stock fraud actions to situations where the market prices of the affected

securities were "grossly unfair", the Court below erred.

POINT IV

THE COURT BELOW ERRED IN FINDING CERTAIN FACTS TO BE MATERIAL WHICH IN ACTUALITY ARE WITHOUT SIGNIFICANCE.

Early in his opinion, Judge Duffy states (103):

> "It should be noted that the 14.9 million dollar after tax re-evaluation represented an unrealized loss, and that even if it had been realized, it would be less than .08% of the defendant's total assets. As a result of market conditions since that time, this loss has been substantially reduced."

In these two sentences are contained three errors of logic (and, therefore, law) which are indicative of the erroneous nature of the opinion below.

(a) What is the materiality of the fact, deemed pertinent by Judge Duffy, that the 14.9 million dollar loss in Chase's bond trading inventory was "unrealized" (in that the depreciated bonds continued to be carried in Chase's inventory and had not been sold)? In presenting a financial statement, or in releasing earnings figures, are "unrealized losses" to be

ignored, thereby misleading the recipients of those figures, including the public? The inclusion of the inflated value of the bonds in Chase's two quarterly statements constituted the misrepresentation complained of in this case, and its materiality is so clear on its face that the Court below erred in shunting this fact aside.

(b) What is the materiality of the fact, deemed pertinent by Judge Duffy, that the loss "if realized" would only constitute .08% of the defendant's "total assets"? The relating of the unrevealed bond trading loss to assets is meaningless. In the case at bar, the significance of the unrealized loss is its relationship to Chase's earnings because market prices of equity securities are primarily affected by and respond (in differing degrees) to the rise and fall of those earnings. The unrevealed losses not only reduced Chase's previously reported earnings by a great deal more than .08%, but they completely wiped out Chase's previously reported significant earnings gains (53). That the revelation of these facts would cause a drop in the market prices of Chase's equity securities is not only understandable, but predictable.

Judge Duffy's light treatment of this "unrealized" loss was not shared by Mr. David Rockefeller, Chase's Board Chairman, who stated that "extremely serious errors of judgment had been made" (54), who instituted additional controls to bar repetition (54) and who, in effect, fired a senior vice-president at the bank because of the misevaluation (54).

(c) Judge Duffy deems material the fact that the subsequent rise in the market prices of Chase's bond inventory erased the earlier unrevealed losses. But, the subsequent recapture of market losses does not retroactively cure the misstatements in Chase's earlier financial statements. Chase's financial statements were still inaccurate at the time they were made, and the market prices for Chase's three equity securities were consequently overvalued at that time. It is that earlier overevaluation in the market prices of Chase equity securities which are the damages plaintiff and the class he represents suffered.

Further in his opinion (105-106) Judge Duffy quotes himself on the role that "hunch" and the "whims and caprice of the crowd" have in determining

market prices for securities.*

Although these factors do affect market prices of securities, that is not to say that an action is not maintainable where market reaction, as here, is clear and convincing. To the contrary, Prof. Bromberg recognizes market reaction as a proper indicator of damages sustained. (see page 15 of this Brief).

POINT V

A FORTUITOUS SUBSEQUENT RISE IN THE MARKET PRICE OF THE CHASE EQUITY SECURITIES CANNOT SHIELD DEFENDANT FROM ANSWERING IN DAMAGES FOR IT'S WRONGDOING.

Judge Duffy's emphasis on plaintiff's "paper

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*We should like to note, parenthetically, that this opinion was one of two Judge Duffy rendered in the litigation arising from Gulf & Western's tender for A & P stock. In a related opinion in that litigation, Lowenschuss, etc. v. W.J. Kane, et al, 367 F. Supp. 911, 917, one of the grounds upon which Judge Duffy dismissed the complaint was that he found, at an early pleadings stage, no damages. This Court reversed (Lowenschuss v. W.J. Kane, not yet reported, Docket Nos. on appeal 74-2156 and 74-2116, decided May 27, 1975) commenting that Judge Duffy's "reasoning with repsect to the absence of damages ... is unclear..."

profits" leaves no guesswork as to the rationale of his opinion: if plaintiff's purchase price for his securities is less than the price at which he sells them, or, if not sold, less than their market value at the time the motion is heard, the plaintiff does not suffer any damages. This Judge Duffy said, is so, regardless of the amount plaintiff may have overpaid for the securities at the time he purchased them as a result of the misleading information then extant.

There is a line of developing law in this field of measurement of damages which point to the error in Judge Duffy's reasoning.

In Janigan v. Taylor, 344 F. 2d 781 (1st Cir., 1965) cert. denied 382 U.S. 879, the Court of Appeals enunciated the rule that in a defrauded seller situation, the defrauding purchaser is liable not only for the difference in value between the price he paid for the securities and their actual value at the date of the transaction, but also any windfall profits reaped by the defrauding purchaser in a subsequent sale of the securities involved. In Janigan, the real value of the securities at the date of sale was established by the price agreed upon between the defrauding purchaser and a third party for the sale of the same securities. Those negotiations never

resulted in a sale. However, some time later the defrauding purchaser sold the same securities to a fourth party at a still higher price.

The Court of Appeals for the First Circuit held that as between the defrauded seller and the defrauding purchaser, the windfall profits on the subsequent sale belonged to the innocent seller. The defendant was therefore required (a) to pay as damages not only the difference between the price paid to the defrauded seller and the real value of the securities at the time of that transaction, but, also, (b) to disgorge the windfall profits that the wrongdoer subsequently received. This holding was specifically approved by the Supreme Court in Affiliated Ute Citizens v. United States, supra. See also, Myzel v. Fields, 386 F. 2d 718, 748-749 (8th Cir. 1967) cert. denied 390 U.S. 951.

In Zeller v. Bogue Electric Manufacturing Corporation, 476 F. 2d 795, 801 (2d Cir. 1973) this Court held that in applying the damages rule requiring the defrauder to disgorge its windfall profits, there should be no distinction between a defrauded purchaser and a defrauded seller. To the same effect see, Ohio Drill & Tool Co. v. Johnson, 498 F. 2d 185, 191 (6th Cir. 1974).

The rationale of this line of cases is that as between the defrauded party and the wrongdoer, the wrongdoer should not reap benefits of a later fortuitous windfall relating to the same securities.

In the instant situation, although the defendant is neither a purchaser nor seller, it stands accused of acts constituting violations of the anti-fraud provisions of Sec. 10 b and Rule 10 b-5. Cast in this posture, defendant nevertheless argues that a fortuitous subsequent rise in the market prices of its equity securities should nevertheless constitute a windfall to it to be used to shield defendant from the consequences of its own wrongdoing. And Judge Duffy, in pointing to plaintiff's alleged "paper profits" months after the curative disclosure, has permitted defendant to use that "windfall" rise in market prices to insulate defendant from having to respond in damages.

POINT VI

THERE WAS NO WAIVER OF PROOF OR A TRIAL IN THE COURT BELOW.

In his opinion, Judge Duffy stated (101-102):

"a suggestion was made that some expert testimony be taken to inform the Court as to the

> workings of the 'stock market'....for some unstated reason the parties agreed to waive any such offer of proof."

On plaintiff's motion, pursuant to Rule 6(b), seeking enlargement of plaintiff's time to make a motion for reargument, plaintiff's counsel denied having agreed to waive any offer of proof (81-83). Indeed, Judge Duffy's recollection of what happened at oral argument is not only at variance with that of plaintiff's counsel, but on a significant point at variance with the recollection of defendant's counsel who stated in his affidavit on the motion for reargument (91):

> "Although I recall no specific offer of expert testimony to inform the Court as to the workings of the stock market..."

Thus we have a situation where the recollections of the Judge and both counsel on this important point all differ.

Unfortunately, there was no Court reporter present while this supposed waiver of proof and of a trial took place. A waiver of such magnitude, if it had been made, should at the least have been taken down by a Court stenographer, and not entrusted to the faulty and conflicting memories of Judge and counsel. A written record not only helps to ascertain the correctness of the recollection of the different

parties, but also to protect the litigants against a Court foisting upon them supposed stipulations to which they, or either of them, in fact, never agreed.

POINT VII

THERE ARE TRIABLE FACTUAL ISSUES ON THE QUESTION OF DAMAGES WHICH PRECLUDE SUMMARY DISPOSITION OF THE CASE ON MOTION.

Judge Duffy's opinion, by his own characterization, was a Rule 52 findings of fact and conclusions of law. Judge Duffy therefore determined that factual questions as to damages (the only issue before him) existed. Such factual issues can only be determined after a plenary trial and not an oral argument on a motion.

Judge Duffy recognized the need for expert testimony to interpret market activity as it bore on the question of damages. Judge Duffy erroneously believed that such essential proof had been waived by the parties.

In view of the conceded need for such testimony, it was incumbent on the Court to affirmatively order a hearing so that a determination of the issue of damages could be properly and intelligently made.

POINT VIII

PLAINTIFF'S WAIVER OF A JURY WAS NOT BINDING BECAUSE IT WAS NOT MADE IN ACCORDANCE WITH THE PROVISIONS OF RULE 39.

Rule 39 of the Federal Rules of Civil Procedure, 28 U.S.C.A. Fed. Rules Civ. Proc., states:

> "When trial by jury has been demanded as provided in Rule 38, the action shall be designated upon the docket as a jury action. The trial of all issues so demanded shall be by jury, unless (1) the parties or their attorneys of record, by written stipulation filed with the court or by an oral stipulation made in open court and entered in the record, consent to trial by the court sitting without a jury..." [Emphasis added].

In the instant proceeding there was no court stenographer making a record of colloquy at the hearing of the motion. The parties, in response to the Court's inquiry, waived the making of such a record. Consequently, the oral waiver of a jury, not being entered in the record as required by Rule 39, was not binding on either of the parties.

In his treatise entitled Law of Federal Courts (West Publishing Company, 1970), Professor Charles Wright, in speaking of a demand for trial by jury, at page 409, writes:

> "Failure to make a timely demand for jury trial waives the right to this form of trial, though the court has discretion, on

motion, to order jury trial despite the waiver."

If the Court has the discretion to order a jury trial even though the party seeking it failed to make a timely demand, a fortiori, the Court has the discretion to relieve a party of its waiver of a jury trial. In the instant situation the setting aside of the waiver of a jury trial would be in the interests of justice, especially where the Court below has already reached conclusions on the ultimate facts.

CONCLUSION

The judgment dismissing the action should be reversed and vacated, and plaintiff granted a trial by jury.

Respectfully submitted,

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Attorneys for Plaintiff-Appellant

On the brief,

GABRIEL KASZOVITZ
MURRAY L. SKALA

SERVICE OF 2 COPIES OF THE WITHIN

Appellants Brief

IS HEREBY ADMITTED.

DATED: August 26, 1975

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